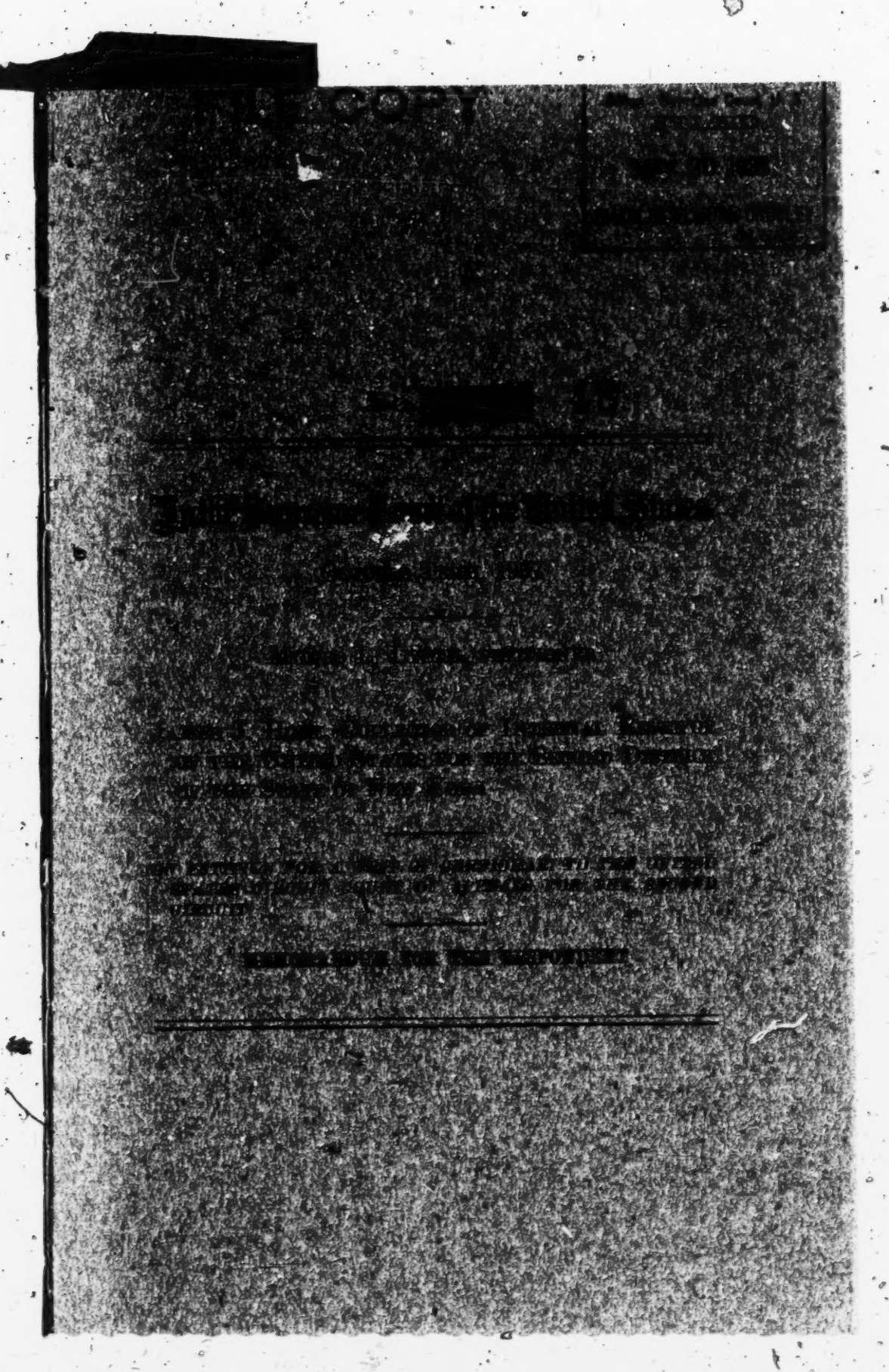

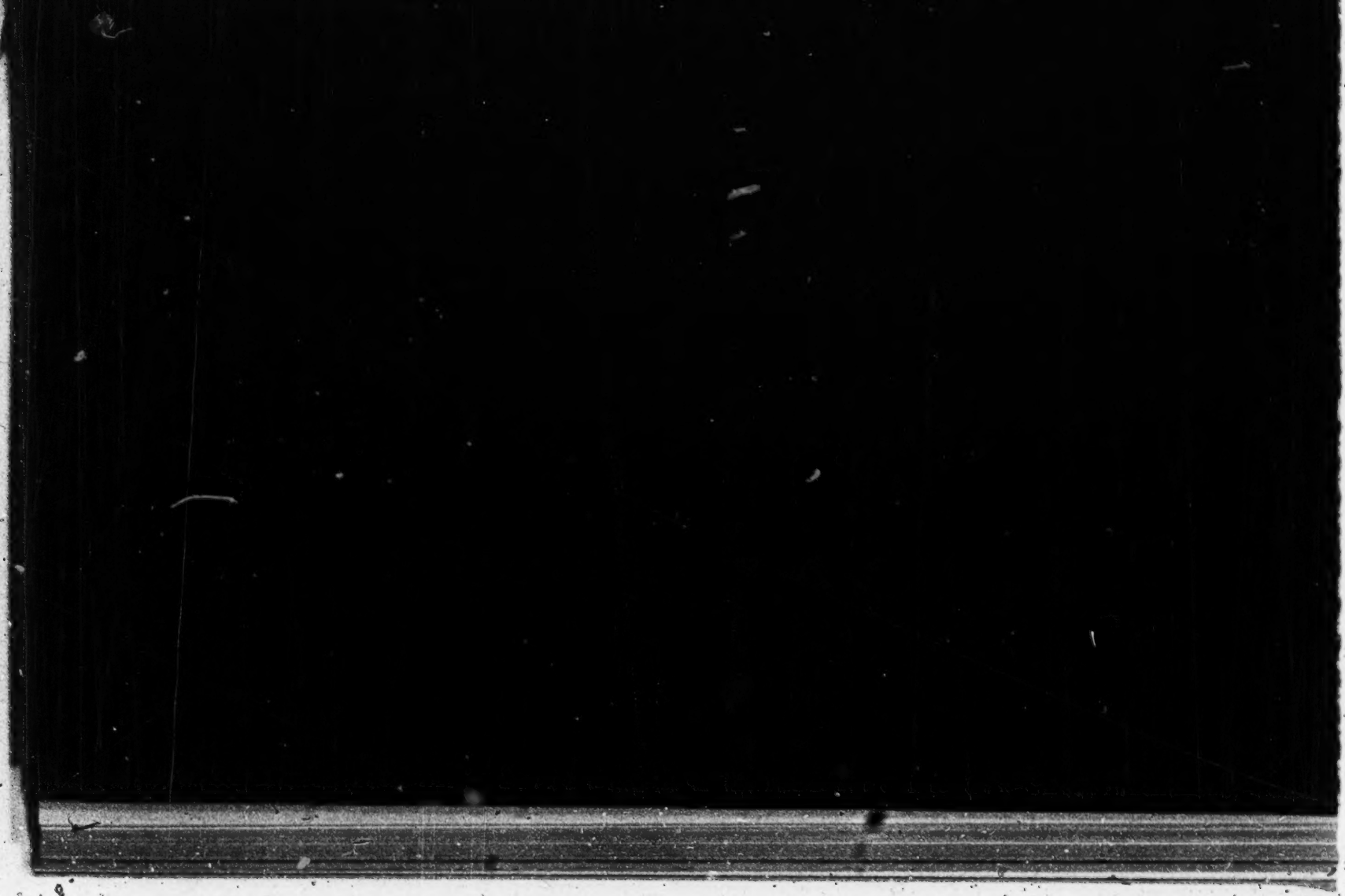

In the Supreme Court of the United States

OCTOBER TERM, 1937

No. 1042

MUNNO L. LYETH, PETITIONER

v.

JAMES J. HOEY, COLLECTOR OF INTERNAL REVENUE OF THE UNITED STATES FOR THE SECOND DISTRICT OF THE STATE OF NEW YORK

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

We do not oppose the granting of the petition for a writ of certiorari in this case.

The case involves the question whether the value of property received by an heir in settlement of a will contest constitutes taxable income.[1]

[1] The court below did not find it necessary to pass upon the alternative issue of recoupment raised by the Government as an affirmative defense. The Government argued that if the court should hold that no tax was due for the reason that the property received by the taxpayer was an inheritance or bequest, the equitable doctrine of recoupment would prevent recovery of a refund for the reason that as

68213—38

The taxpayer is a grandson of Mary B. Longyear, who died on March 14, 1931, a resident of Massachusetts (R. 90). By her will the testatrix bequeathed small legacies to the taxpayer and others, but left the residue of her property, constituting the bulk of her estate, to a charitable trust (R. 51–61, 91). The heirs objected to the probate of the will on several grounds, including a lack of testamentary capacity and undue influence, and, in accordance with the applicable law of Massachusetts, moved in the probate court that jury issues be framed in order that the validity of the will might be determined by trial by jury (R. 91–92). The motion was granted (R. 92), but before the case was tried all the parties in interest entered into an agreement of compromise (R. 24–50) providing for the allowance of the will and the distribution of the estate in accordance with the will and agreement of settlement (R. 96–97).

This settlement was approved by the probate court in a decree which allowed the will, provided for the issuance of letters testamentary to the executors named therein, and directed them "to admin-

---

a transferee of the estate he was liable for an additional estate tax resulting from an excessive deduction for charitable bequests. The additional estate tax arises from the fact that the total value of the bequest to the charitable trust under the will was allowed as a deduction in computing the estate tax, instead of the allowance of a deduction of the amount actually received by the charitable trust under the compromise. (R. 82–85.)

ister the estate of said deceased in accordance with the terms of said will and said agreement of compromise" (R. 62–63, 96–97).

As the result of this compromise the taxpayer in 1933 received property determined by the Commissioner of Internal Revenue to be worth $141,484.03, no part of which was reported as income (R. 14). The Commissioner treated the amount as taxable income and assessed an additional income tax, with interest, in the total amount of $65,005.68, which was paid (R. 17). A timely claim for refund (R. 16–22) was filed and rejected (R. 23) and this suit for refund was instituted.

The District Court gave judgment for the taxpayer.[2] On appeal the Circuit Court of Appeals reversed the District Court, holding that the value of the property received under the settlement constituted taxable income. The majority opinion, written by Circuit Judge Chase, holds that the amount received was a gain growing out of the claim to an interest in property; that what the taxpayer received was an amount received not under the will but in spite of the will because of his bargaining position; and that, as what he relinquished in consideration of the receipt of the property under the settlement had no cost basis, the full value of the property received constituted

[2] The District Court also decided against the Government on the recoupment issue (20 F. Supp. 619, 622). See footnote 1, *supra*, p. 1.

taxable income. The court held further that under Massachusetts law an heir who takes under a compromise settlement of the character of the one here involved is regarded as taking by purchase from those who get title under the allowed will; and hence that the value of the property is not exempt as a bequest or inheritance under Section 22 (b) (3) of the Revenue Act of 1932, c. 209, 47 Stat. 169.

Circuit Judge Augustus N. Hand concurred in a separate opinion on the ground that there was no proof that the sum received by the taxpayer in settlement of a will contest was not wholly gain over the value of any right which passed to him on the death of the testatrix; and expressed the opinion that if it had been or could have been shown what the rights of the next of kin to contest the will were worth only the excess received over that value would be taxable income.

The decision of the court below is in accord with the decision of the Board of Tax Appeals in *Kearney* v. *Commissioner*, 31 B. T. A. 935, and is supported by the decision in *Sterling* v. *Commissioner*, 93 F. (2d) 304 (C. C. A. 2nd), certiorari denied, April 11, 1938, No. 839, present Term, which involved an analogous but not identical question.

The petition for a writ of certiorari alleges that the decision of the court below is in conflict with the decision of the Circuit Court of Appeals for the Fourth Circuit in *Magruder* v. *Segebade*, 94 F. (2d) 177. We agree that these decisions cannot be

distinguished. In the *Segebade* case the court held that an amount received in compromise of a will contest was not income. In that case the taxpayers were legatees under two wills made by the decedent, a resident of Maryland, and in consideration of the receipt of a lump sum they agreed to waive their rights under the first will and not to contest the second which was filed for probate. The court held the amount received was not income under the Sixteenth Amendment and the statute involved and found it unnecessary to consider whether it was exempt as a bequest or inheritance. The payment to the taxpayers was made by the residuary legatees in the *Segebade* case, whereas in this case it was made by the executors pursuant to the order of the probate court; but this distinction is not believed to be material in determining whether an amount received in settlement of a will contest constitutes income. The decision of the District Court in the instant case was relied upon by the Circuit Court of Appeals for the Fourth Circuit in the *Segebade* case, and in the instant case the court below did not distinguish the *Segebade* case.

By reason of this conflict and of the general importance of the question we do not oppose the granting of the petition.

Respectfully submitted.

ROBERT H. JACKSON,
Solicitor General.

MAY 1938.

U. S. GOVERNMENT PRINTING OFFICE: 1938